

Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See 86 Ill. Adm. Code 130.220. (This is a PLR).

November 29, 1999

Dear Ms. xXXXX

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (see enclosed), is in response to your letter of October 18, 1999. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter, you have stated and made inquiry as follows:

I am requesting a private letter ruling regarding the below information:

We are a leasing company located outside the state of Illinois with no offices or employees located within your state. We lease office equipment such as copiers, faxes, computers, telephones and related equipment. We realize on rental or fair market value leases, tax is to be paid to our dealer. We do comply with this rule but my question is, when the dealer invoices us for the equipment, depending on the lease program, maintenance is also included in the price but is a separate line item on their invoice. Is tax due on the equipment price only or on both the equipment and the maintenance? On a conditional sales lease (\$1.00 buyout) we have previously been told by the state, tax is due on each monthly rental payment we receive from the lessee. We bill the customer one flat monthly payment. On these special programs that have maintenance, the lessee is unaware how much of their payment is for the equipment and how much is for the maintenance. For example we will bill the customer a \$250.00 monthly lease payment plus applicable taxes. (\$200.00 for the equipment + \$50.00 maintenance fee). Once the maintenance fee is collected from the lessee, we remit it back to our dealer to cover his costs of the upkeep of the machine. Should we be taxing the maintenance portion of the lease payment?

Also is freight or installation fees taxable on any type of lease when they are separately stated on the invoice from the dealer to us?

I have enclosed a copy of the power of attorney form that has previously been remitted to your office. You should have the original on file. We had a private letter ruling issued to us in the past regarding the sales tax treatment of different lease types and when the tax is due. Please forward us a copy of that letter and your response. Your help is greatly appreciated so we can abide by the Illinois state tax laws. If you need further information, please contact me at the above address or telephone number. Thank you for your time and cooperation.

As you know, the State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if lessors are guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction, thus making all receipts subject to Retailers' Occupation Tax.

In regards to conditional sales, the taxability of maintenance agreements is dependent upon whether the charge for the agreement is included in the selling price of tangible personal property. If the charge for a maintenance agreement is included in the selling price of tangible personal property, that charge is part of the gross receipts of the retail transaction and is subject to Retailers' Occupation Tax liability. No tax is incurred on the maintenance services or parts when the repair or servicing is completed.

If maintenance agreements are sold separately from tangible personal property, the sale of the agreement is not a taxable transaction. However, when maintenance services or parts are provided under the maintenance agreement, the company providing the maintenance or repair will be acting as a service provider under the Service Occupation Tax Act. The Service Occupation Tax Act provides that when a service provider enters into an agreement to provide maintenance services for a particular piece of equipment for a stated period of time at a predetermined fee, the service provider incurs Use Tax based upon its cost price of tangible personal property transferred to the customer incident to the completion of the maintenance service. See 86 Ill. Adm. Code 140.301(b)(3), enclosed. This is because the service provider, in these instances, is the user of the tangible personal property, not because he has elected to be de minimis.

In the conditional sale situation you describe in your letter, your company is billing the customer one flat monthly payment which includes both an amount for the equipment that was conditionally sold and an amount for the maintenance agreement. The customer does not know how much is attributable to each item. In this situation, the total amount of the monthly payment is part of the gross receipts of the retail transaction and is subject to Retailers' Occupation Tax liability. No tax is incurred on the maintenance services or parts when the repair or servicing is completed.

A true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true

lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See the enclosed copy of 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability. Please note that the above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

Whether you need to pay tax on the maintenance charge that you are assessed by the dealer when you purchase equipment that will be leased under the provisions of a true lease depends upon if the charge is part of the total cost or a separate agreement. See 86 Ill. Adm. Code 140.301. You state that when you purchase the equipment from the dealer that the maintenance charge you pay is separately stated. We are assuming from your representation that the maintenance charge is separately stated because you have entered into a separate maintenance agreement with the dealer. This being the case, you owe no tax to your dealer on the maintenance charge for the equipment you are purchasing to lease under a true lease agreement. However, as stated above, when maintenance services or parts are provided under the maintenance agreement, the company providing the maintenance or repair will be acting as a service provider under the Service Occupation Tax Act.

You have asked about freight and installation charges. We are assuming that you are requesting information regarding the transaction where the dealer sells the tangible personal property to you for lease under a true lease. As a technical proposition, handling charges represent a retailer's cost of doing business, and are consequently always included in gross charges subject to tax. See, 86 Ill. Adm. Code 130.410. However, such charges are often stated in combination with shipping charges. In this case, charges designated as "shipping and handling," as well as delivery or transportation charges in general, are not taxable if it can be shown that they are both separately contracted for and that such charges are actually reflective of the costs of shipping. To the extent that shipping and handling charges exceed the costs of shipping, the charges are subject to tax. As indicated above, charges termed "delivery" or "transportation" charges follow the same principle.

The best evidence that shipping and handling or delivery charges have been contracted for separately by purchasers and retailers are separate contracts for shipping and handling or delivery. However, documentation that demonstrates that purchasers had the option of taking delivery of the property, at the sellers' location for the agreed purchase price, plus an ascertained or ascertainable delivery charge, will suffice. If retailers charge customers shipping and handling or delivery charges that exceed the retailers' cost of providing the transportation or delivery, the excess amount is subject to tax.

Please be advised that when tangible personal property is sold at retail and the seller installs such tangible personal property for the purchaser, the installation charges are included in gross receipts subject to tax unless they are subject to a separate agreement. A separate agreement would include an invoice that separately lists the installation charge and is also signed by the customer. See 86 Ill. Adm. Code 130.450, enclosed.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

I hope this information is helpful. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.